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SUBJECT: MONTENEGRO: ECONOMIC DEVELOPMENTS: MAY 2006

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MACROECONOMICS:

Montenegro Declares Independence From Serbia

1. On June 3, the Parliament of Montenegro adopted a Declaration of Independence, following the May 21 referendum on independence from Serbia. The two economies were already distinct, stemming from Montenegro's adoption of the deutsche mark in 1999, and later the Euro. The distinction is reflected by the separate applications of Montenegro and Serbia to the WTO, and the EU's "twin-track" approach on accession. The GoM has posted on its website, www.vlada.cg.yu/eng, the May 21 Financial Times article, "Montenegro can seize its chance to be friendly to business," underscoring its commitment to economic reform and investment.

2. Deputy Prime Minister Branimir Gvozdenovic, speaking in Belgrade at both the May 11 Summit of Serbia and Montenegro, and before the American Chamber of Commerce on May 31, said Serbia will remain as Montenegro's most important economic partner. He stressed that business relations will break down any barriers that politicians may attempt to erect. Local business associations, the Montenegro Business Alliance (MBA) and the Association of Employers of Montenegro (UPCG), also welcomed independence

as good for development and for business. Standard and Poors confirmed that the referendum would have no negative effect on its rating for Montenegro, raised to BB-plus in December 2005.

Indicators for Q1 2006

¶3. GDP rose 4.1 percent in real terms in first quarter. Industrial production rose by 4.4 percent, while tourism and catering marked a sharp increase of 25.9 percent. A slow-down in aluminum production at KAP in April however resulted in a decrease in monthly overall industrial production, down 7.8 percent from a year earlier. The GOM's budgetary deficit was held to 1.5 percent of GDP. Inflation is on target to meet the annual goal of no more than 3 percent, with inflation through the end of April at 1.1 percent.

Export Tariffs to be Abolished

¶4. Minister for Foreign Economic Relations Gordana Djurovic announced that all export tariffs will be abolished by January 1, 2007, in accordance with WTO standards.

IMF, Montenegro Express Readiness for Cooperation

¶5. Finance Minister Igor Luksic said Montenegro will establish full relations with the IMF, World Bank, European Bank for Reconstruction and Development (EBRD), and similar institutions. With the IMF, it will draw a new program of cooperation, focused on structural reforms. The IMF Resident Representative replied that the IMF was ready to cooperate with Montenegro.

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BUSINESS and TOURISM:

KAP: Strike Threat

¶6. Rusal, the new owners of Kombinat Aluminum Podgorica (KAP), are looking to cut costs by reducing overstaffing. KAP offered excess staff severance pay, computed as 6 month's pay for executives, 12 months for part-time workers and "privileged" workers, 10 months for all others. The KAP labor union responded by asking that all discharged workers receive 24 months severance pay. In late March, the Union announced it would organize a strike, citing postponement by the new owner of talks to reconcile the positions. The commencement of the strike has been repeatedly postponed, and is still on hold. KAP estimates a strike could cost USD 100,000 per day.

New Airports

¶7. Podgorica Airport opened its new, Euros 22 million, terminal on May 14. The modernized Tivat terminal, which received an eight million Euro investment, will open in early June.

Tourism Numbers up Through April

¶8. Through the end of April, 58,600 tourists had visited Montenegro, up 23 percent over the same period in 2005. Foreign tourists were up 42 percent to 25,000.

Best Western Opening in Podgorica

¶9. The U.S.-based Best Western chain will open its first

hotel in Montenegro in June, when local franchisors open a 48-room hotel in Podgorica.

PUBLIC ECONOMY:

Unemployment Down

¶10. The GoM said unemployment declined 1.2 percent to 17.46 percent. Unemployment this time last year was 21.5 percent.

Montenegro to Pay Off Old Foreign Exchange Deposits

¶11. The Government of Montenegro announced in mid-May that it would repay citizens of Montenegro who had deposited foreign exchange in Serbian banks. The total amount on deposit reported to date is Euros 19.7 million.

Private Savings Deposits Nearly Double

¶12. In the past twelve months, private savings deposits in Montenegrin banks increased by 71 percent, to Euros 198.2 million by the end of March, 2006.

Real Wages Rise

¶13. The average net monthly wage in April was Euros 246, up 4.3 percent from March, with real wages rising 3.6 percent. Retail prices rose 0.6 percent, and the consumer basket for a family of four rose 0.2 percent to Euros 267. (MonStat data)

T-BILLS

¶14. Two auctions of Treasury bills, with a total face value of EUR 1.7 million, was held in April (note: data lags by one month). The average weighted annualized interest rate for the auction held in March amounted to 2.52 percent. The lowest accepted interest rate at the auctions held in April was 0.75 percent while the highest accepted interest rate was 5.00 percent. Participants at the auctions included local banks.

STOCKS

¶15. The NEX20 index of the Nex Montenegro Stock Exchange ended the month of May up 16.7 percent, at 12,316.56. The

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Moste index of Montenegroberza rose 18.0 percent to 569.732 in May. The sharp rise reflected support from local investors for independence, which they expect will expand economic opportunities and attract further investment. Major components of the NEX20 include the privatized Telekom CG and Jugopetrol; major components of the Moste include aluminum smelter KAP and vineyard Plantaze. Note: The Montenegrin exchanges are still nascent, and the level of capitalization represented is small although rising (NEX capitalization at the end of 2004 was Euros 45 million; at the end of November 2005 it was Euros 1,410 million).

MOORE